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CYNICAL BREACHES OF RESTRICTIVE COVENANTS AND SECTION 84 LPA APPLICATIONS

Alexander Devine Children's Cancer Trust v Housing Solutions Limited

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The Supreme Court has upheld the decision in the Court of Appeal that the application under section 84 LPA 1925 to modify the restrictive covenants should fail because the developer had deliberately breached the covenant. However, the judgment of Lord Burrows on behalf of all the Law Lords was more nuanced and has adopted a significantly different approach to that adopted by the Court of Appeal and in particular Sales LJ.

1. Restrictive covenants – these was imposed when a farmer owning land near Minehead situate in the Green Belt sold an area of open land to a neighbouring industrial concern in July 1972. In the conveyance restrictive covenants were included providing that

(i) No building structure or other erection of whatsoever nature shall be built erected or placed on the purchased land.

(ii) The purchased land shall not be used for any purposes whatsoever other than as an open space for the parking of motor vehicles."

This was imposed for the benefit of the land owned by the farmer situated within three quarters of a mile of the encumbered land.

2. Objective – at that time it appeared that the objective of the restrictive covenant was to protect an overage provision which entitled the farmer to 75% of the uplift in the value of the land sold if planning permission was granted for any purpose other than parking. Once the payment was made the land would be automatically released from the restrictive covenant. This overage provision was subject to a time limit of twenty-one years from the date of the conveyance. The significance of the overage aspect is discussed in section 11 below.

3. Background – the twenty-one year period expired so that the overage entitlement was extinguished but that meant that with it went the ability to obtain a release. The farm land with the benefit of the restrictive covenants passed to the son on the death of the original farmer and at the end of 2011 the son obtained planning permission in relation to part of the land next to the encumbered land for the construction of a hospice for children with terminal cancer and their carers. Following this the son gifted this land to a charity.

Millgate Developments Limited ("Millgate") acquired the encumbered land in 2013 together with the unencumbered adjoining industrial site. It did so knowing of the existence of the restrictive covenants. Millgate then applied for planning permission to build 23 affordable housing units on the combined site. This was linked to an application for planning permission to build 75 housing units on a different site. Both applications were granted with the authorisation for the development of the other site being conditional on the provision of the affordable housing on the combined site. Millgate gave a unilateral declaration pursuant to section 106 TCPA 1990 that not more than 15 units on the linked site would be constructed until the 23 affordable units had been transferred to an affordable housing provider.

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Millgate's plans for the affordable units allocated ten in a block of flats on the unencumbered part of the combined site and nine houses and four bungalows were to be constructed on the encumbered land. It was found by the Upper Tribunal that if Millgate had allocated all 23 affordable units to the unencumbered part of the combined site and car parking to the encumbered land this would have been accepted by the local planning authority and complied with the restrictive covenant.

Millgate begun clearing the site on 1st July 2014 and the son first became aware of the planning permission and the work at the end of August 2014. Despite vigorous objections being made on behalf of the son the work continued and was completed on 10th July 2015. The upper floors of the houses overlooked the hospice grounds and their gardens backed onto those grounds. The roofs of the bungalows were visible from the hospice land.

On 20th July 2015 Millgate applied for a modification of the restrictive covenants to allow the already constructed houses and bungalows to remain and be occupied. This was objected to and the litigation commenced leading so far to the Supreme Court via the Upper Tribunal and the Court of Appeal but with the possibility of more litigation to come. The unencumbered part of the combined site was transferred to Housing Solutions. Subsequently, the encumbered land was transferred to Housing Solutions on 15th February 2015.

No application has been made for an injunction although one was threatened after the Court of Appeal decision. This was countered by a threat to apply for a stay whilst these proceedings were continuing. This aspect of the matter will either be resolved by a negotiated settlement or further proceedings.

4. Section 84 LPA – there are five grounds conferring jurisdiction on the Upper Tribunal to discharge or modify restrictive covenants. This case is concerned with the ground set out in section 84(1)(aa) and (1A)(b) – the "contrary to public interest" ground. It applies if

(i) the continued existence of the restrictive covenants would impede some reasonable user of the land for public or private purposes or would do so unless modified (subs. (1)(aa)); and

(ii) the Upper Tribunal is satisfied that the restriction in impeding such reasonable user "is contrary to the public interest" provided that money will be an adequate compensation for the loss of disadvantage which any person entitled to the benefit of the restrictive covenants will suffer from the discharge or modification (subs. (1A)(b)).

The first stage in the consideration of an application requires a decision as to whether there is jurisdiction to discharge or modify. If one of the grounds is satisfied then the second stage is whether the Upper Tribunal should exercise its discretion.

As regards the "contrary to public interest" ground it was stated by Mr. Frank (as he then was) in re Collins Application that in "my view, for an application to succeed on the ground of public interest it must be shown that that interest is so important and immediate as to justify the serious interference with private rights and the sanctity of contract." The continuing validity of this statement has been left in some doubt following this decision.

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5. Section 84(1B) – in deciding whether one of the statutory grounds have been satisfied thereby conferring jurisdiction on the Tribunal this sub-section requires account to be taken of any development plan and "any declared or ascertainable pattern for the grant or refusal of planning permissions in the relevant areas." This is the main emphasis of the provision but it goes on to say "as well as the period at which and context in which the restriction was created or imposed and any other material circumstances." Interestingly there was no discussion in this context of the automatic discharge of the restrictive covenants in the event of a grant within the specified twenty-one year period and payment of an agreed overage sum.

What was made very clear was that the words "any other material circumstances" do not mean all the circumstances relating to the application but only those concerning whether or not one of the statutory grounds has been satisfied. That means in this matter only circumstances relevant to whether impeding the reasonable user by the continuation of the restrictive covenants is contrary to the public interest.

6. Upper Tribunal - it was found that the residential development on the encumbered land would have little visual impact inside the hospice but would be greater in the grounds. Even if the cautious approach put forward in Re Collins still applies the Tribunal placed great weight on the immediate public interest in not losing much needed affordable housing and considered that "contrary to public interest" ground was made out as in the judgment of the Tribunal the payment of £150,000 for the cost of remedial planting and loss of amenity would adequately compensate the charity.

It then considered the discretion it had and notwithstanding the behaviour of Millgate being characterised by it as "highhanded and opportunistic" this was outweighed by the public interest which was described as "an unconscionable waste of resources for these houses to continue to remain empty". Lord Burrows used the phrase "cynical breach" "as a useful shorthand description of the conduct of Millgate in deliberately committing a breach of the restrictive covenant with a view to making a profit from so doing."

7. Court of Appeal – this decision was set aside and was replaced by a refusal of the application. It was held that the Upper Tribunal in deciding both whether it had jurisdiction to make the modification and also in exercising its discretion had failed to properly take into account the "cynical breach" by Millgate.

8. Jurisdiction – in the Supreme Court the argument as to whether the "contrary to public interest" ground had been satisfied centred on the interpretation of that phrase. Lord Burrows stated that when considering whether impeding the reasonable user of the land by the continuation of the restrictive covenant is contrary to the public interest it "is of central importance that the question that has to be asked is not the wider one of whether in all the circumstances of the case it would be contrary to the public interest to maintain the restrictive covenant. Rather the wording requires one to focus more narrowly on the impeding of the reasonable user of the land and to ask whether that impediment, by continuation of the restrictive covenant, is contrary to the public interest."

Contrary to the approach adopted by the Court of Appeal it was held that "the good or bad conduct of the applicant is irrelevant at this jurisdictional stage". At that stage the considerations to be taken into account were limited to the public interest in not wasting housing to be set against the public interest in providing a hospice with the continuing protection of the restrictive covenants. As Lord Burrows described it "two competing uses of the land are therefore pitted against each other."

In consequence the Upper Tribunal's decision on jurisdiction could not be successfully challenged and the Court of Appeal was wrong.

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9. Exercise of discretion – Lord Burrows stressed that in order to succeed on an appeal against an exercise of a discretion it was necessary for there to be an error of law and the appeal court could not merely substitute its own view for that of the decision maker particularly when a specialist tribunal.

The Court of Appeal took the view that the Upper Tribunal had failed to attach sufficient weight to the cynical breach when exercising the discretion and that this constituted an error of law. The Supreme Court stated that it was inappropriate for an appellate court to interfere with a discretionary decision on the ground that it failed to attach sufficient weight to a factor and so it considered that what the Court of Appeal was really saying was that it was contrary to principle to allow an application by a person who has committed a cynical breach. Lord Burrows did not accept such a principle existed as there would need to be qualifications which would not allow the Tribunal's decision to be set aside.

Notwithstanding that the Tribunal had taken into account the cynical breach Lord Burrows considered that something had gone fundamentally wrong. His approach was more nuanced. Despite the cynical breach being taken into account two important factors had not been taken into account. The first was that Millgate could have obtained a planning permission which respected the restrictive covenants by locating all the affordable units on the unencumbered part of the combined site. The second was that if Millgate had respected the rights of the charity by applying for modification before commencing the development then the application would not have succeeded because the affordable housing could be accommodated wholly on the unencumbered part of the combined site. Millgate was seeking to obtain an advantage by presenting the Tribunal with a fait accompli. The public interest point is decided by reference to the facts as at the date of the hearing and not those existing before the breach if earlier. The carrying out of the development meant that the Tribunal would be dealing with land with affordable housing existing on it and not with an open site. The importance of that change having been brought about by the cynical breach was not taken into account by the Tribunal at the discretionary stage.

If the decision had been allowed to stand then it would encourage developers to disregard restrictive covenants and press ahead even in the face of strong objections. The failure to take these factors into account constituted an error of law and so the appeal was dismissed and the application refused after those two omitted factors had bene taken into account along with the factors taken into account by the Upper Tribunal.

10. Scope of decision – the Court of Appeal decision was very clear that a cynical breach is to be taken into account at both the jurisdictional and discretionary stages and would prevent a section 84 application being successful. The Supreme Court decision was equally clear that it could not be taken into account at the first stage concerning jurisdiction but only at the second stage concerning the exercise of the discretion. With the second stage the Supreme Court was more nuanced because it accepted that the existence of the cynical breach did not automatically mean that this section 84 application must fail. The Upper Tribunal's decision to grant the modification would have stood but for the particular facts of this matter. What made the difference was that it was open to Millgate to arrange matters so that the affordable housing was wholly on land which was not subject to the restrictive covenants thereby avoiding the need for the cynical breach and the section 84 application. If it had made the section 84 application before starting the works it would have been rejected and so had no means of avoiding the consequences of the cynical breach.

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With most section 84 applications considered by the Upper Tribunal there will not be such an ability for an applicant to arrange the development so as to achieve the desired outcome whilst at the same time respecting the restrictive covenants thereby avoiding it constituting a breach of the continuing restrictive covenants. That raises the question as to how the Upper Tribunal should take into account a cynical breach when it was not open to the developer to plan the development in a manner which respects the restriction and avoids such a breach. There will also be the separate question whether if the developer has that ability but is relying on a ground other than the "contrary to public interest" ground will a cynical breach have the same affect at the second stage as in this case.

This will require consideration of a number of factors and some will be different to those which applied in this case.

(i) policy behind grounds – the "contrary to public interest" ground was added by the LPA 1969 and the policy behind paragraph (aa) and its supporting provisions was explained by Carnwath LJ (as he then was) in Shephard v Turner : "The general purpose is to facilitate the development and use of land in the public interest, having regard to the development plan and the pattern of permissions in the area. The section seeks to provide a fair balance between the needs of development in the area, public and private, and the protection of private contractual rights". This emphasises that this ground may lead to enforceable and useful restrictive covenants being overridden because it is in the public interest to modify or discharge the restriction.

This rationale is different from the other grounds. In the Law Commission's 1966 Working Paper on Restrictive Covenants it was stated that "The object of s. 84(1) of the L.P.A. 1925 was, in the public interest, to provide a means whereby restrictions on land use or development which are in whole or part substantially dead, can be deprived of their legal basis." Later in 2011 the statutory jurisdiction was described by the Law Commission as conferring the ability to remove restrictive covenants which "are no longer useful".

The differing rationale would suggest that the exercise of the discretion in the second stage may differ dependent on the type of ground conferring jurisdiction. It could be argued that if the restrictive covenants are "dead" or "no longer useful" then jumping the gun by starting the development has no long term impact. In contrast with applications based on the "contrary to public interest" ground such a breach may impact the outcome because it is carrying forward a development which is actually providing a public benefit rather than having the potential to do so.

However, this is not necessarily how cynical breaches will be taken into account when the Upper Tribunal exercises the statutory discretion. There are other factors to also be taken into account.

(ii) general approach to exercise of discretion – there have been statements in Upper Tribunal judgments concerning the exercise of the statutory discretion with regard to a section 84 application when the applicant is in breach of the relevant restrictive covenant. In re George Wimpey Bristol Ltd's Application [2011] UKUT 91 (LC) Mr. Rose FRCIS stated at paragraph 35 that:

"I would add that, if ground (aa) had been made out, it is unlikely that I would have exercised the discretion that I have to modify the covenant. This is because I find on the evidence that the extensive works which Wimpey Homes have carried out on the application land were not an inadvertent action

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resulting from the discovery of the covenant at a late stage in the development programme. Rather, they were the result of a deliberate strategy of forcing through the development on the restricted land in the face of many objections from those entitled to the benefit of the restriction, to the point where they had so changed the appearance and character of the application land that the Tribunal would be persuaded to allow them to continue with the development. It is appropriate for the Tribunal to make it clear that it is not inclined to reward parties who deliberately flout their legal obligations in this way."

This concerned a section 84 application under the first limb of ground (aa) and not the public interest limb of that ground. It was obiter as the claimed ground was not held to have been satisfied. If the claimed ground in that case had been established it would have meant that a restrictive covenant which did not secure benefits of substantial value or advantage would have continued unmodified because of the applicant's breach. As a general approach this seems unduly harsh.

In contrast in re the Trustees of Green Masjid and Madrasah's application it was stated by Mr. Trott FRCIS that:

"128. In my opinion the applicants' conduct justifies Mr Bates's description of it as that of someone "chancing their arm" and constitutes a sustained and wilful breach of the covenant. Such conduct is to be deprecated. Mr Bates referred me to Re George Wimpey Bristol Limited's Application and Re Lee's Application in which the Tribunal said that had ground (aa) had been made out it was "unlikely" that discretion to modify the covenant would have been exercised (Wimpey) and that the objector "would have been likely to argue quite strongly against an order in [the applicant's] favour in the event that [the applicant] had made out a case" (Lee). In both cases the Tribunal based its comments upon the conduct of the applicant. But in both cases these comments were obiter since the Tribunal found that there was no jurisdiction for it to modify or discharge the covenants in any event. In the present application I have found that I do have such jurisdiction.

129. The purpose of section 84 of the 1925 Act is to enable applicants to obtain modification or discharge of restrictive covenants in circumstances where they can demonstrate statutory jurisdiction. Having satisfied me on the facts, and on the law as applied to those facts, that the Tribunal has such jurisdiction in this case, I am loath to exercise my discretion so as to deny the applicants the relief that they seek. Where jurisdiction has been established I consider that the discretion of the Tribunal to refuse the application should only be cautiously exercised. It should not be exercised arbitrarily and, in my opinion, should not be exercised as, effectively, a punishment for the applicants' conduct unless such conduct, in all the circumstances of the case, is shown to be egregious and unconscionable. On balance I do not consider that the applicants' conduct was so brazen as to justify my refusal of their application."

In that matter although both limbs of ground (aa) were relied on it was held that the first limb had been established and so there was no need to decide the public interest ground. The statutory discretion was, therefore, exercised as a result of jurisdiction having been conferred because the restrictive covenant did not secure any practical benefits of substantial value or advantage.

The point is well made in that passage from the judgment of Mr. Trott that in those circumstances to exercise the discretion by refusing the application is to punish the breach. In that case two factors were borne in mind when considering that aspect of the exercise of the discretion. First, the applicants were trustees and had not acted out of self-interest. Second, the applicants had acted under a mistaken belief

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that the grant of planning permission was a solution to the problem. Consequently, it was considered that to refuse the application due to the breach would be disproportionate and unduly harsh.

In SJC Construction Company Limited's application a similar line was taken when it was stated by Mr. Frank QC (as he then was) that "I am satisfied, as I think are the Council, that they acted in good faith in the sense that they did not intend to force the Council's hand."

The deliberate commencement of development ahead of a section 84 application based on a calculation that an advantage will flow from this step has been regarded differently to cases in which the development has been commenced due to a mistaken belief that there was no opposition or the grant of planning permission overrides the restrictive covenants.

(iii) grounds other than "contrary to public interest" – it was stated by the Upper Tribunal in the Alexander Devine Children's Cancer Trust case that if the section 84 applications had been based on grounds other than "contrary to the public interest" then it would have been harder for it to exercise the discretion in favour of modification. It was existence of a strong public interest in having the completed affordable housing units retained which swayed the upper tribunal to accede to the application. Without that public interest it would have increased the importance of the need to avoid encouraging developers to commence development before an application is made.

Should the existence of a cynical breach in such circumstances mean that a modification or discharge should be refused in exercise of the Tribunal's discretion? The Supreme Court has made clear it is not a rule that a cynical breach will automatically require an application to be refused. If a restrictive covenant ought to be deemed obsolete and so falls within ground (a) should a cynical breach stand in the way of a modification or discharge which would have been granted if the application had been made before the development commenced. The same point arises if the proposed modification or discharge has been expressly or impliedly agreed (ground (b)) or will not injure the persons entitled to the benefit of the restrictive covenant (ground (c)) or the restriction does not secure to persons entitled to the benefit of it any practical benefit of substantial value or advantage (first limb of ground (aa) and (1A)(a)).

In all of such circumstances does the cynical breach affect the relevant circumstances to be taken into account or what has to be determined or impact the outcome? It would seem unlikely and so if the discretion is exercised by rejecting the proposed modification or discharge it is to so as to discourage such breaches. The tenor of the judgment of Lord Burrows does not support such an approach. There is no absolute rule that a cynical breach will cause the application to fail. Failing to respect the Tribunal's statutory jurisdiction is important but need not necessarily prevent an appropriate modification or discharge being ordered.

(iv) "contrary to public interest" ground - when there is a section 84 application based on the "contrary to public interest" ground but there had been no ability to carry out the development in a manner which did not breach the relevant restrictive covenant it will be harder to predict the outcome of the exercise of the discretion. Lord Burrows did not consider that but for the omitted two factors arising from the ability to locate the affordable housing on land not subject to the restrictive covenants the Upper Tribunal's exercise of the discretion would have been an error of law. It is open to the Upper Tribunal to reach the same conclusion as it did in this case and to make the appropriate modification or discharge.

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It will be open to each Tribunal to reach its own judgment regarding the exercise of the discretion based on the particular facts of the case. It is entitled to conclude that the public interest element outweighs the existence of a cynical beach.

(v) Caution – what the Supreme Court decision does serve to emphasise is the need for care on the part of developers when developing sites subject to restrictive covenants. To press ahead and not take their existence into account runs the risk of costly litigation, a halted development or at worse even the making of a mandatory injunction to demolish work already carried out.

11. **Overage** – the fact that the restrictive covenants were imposed to protect an overage agreement providing for an automatic release of those restrictive covenants upon payment of the overage played no substantive role in this litigation. It was noted by the Tribunal. Thereafter there was no discussion of this in any of the judgments. Once the overage arrangement had expired the restrictive covenants were treated as normal restrictive covenants.

The circumstances of the case with regard to the overage arrangement serves to highlight difficulties arising from the use of restrictive covenants as a means of protection.

(i) Expiry of overage arrangement – when there is a limited overage period but the duration of the restrictive covenant is not also limited but continues after the expiry of the overage period that can pose problems for the owner of the land subject to the restrictive covenant. That owner will have lost the benefit of the automatic release provision if one is included in the overage arrangement. The expiry of the overage period will confer the unfettered power on the person entitled to the benefit of the restrictive covenant to enforce it or seek a negotiated payment for its release as is now the position in this case.

(ii) Risk of modification or discharge – the protection provided by a restrictive covenant is not an absolute protection there is a risk of a section 84 application. Any compensation awarded when a modification or discharge is ordered will not include an amount representing the loss of the opportunity to negotiate a release of the restrictive covenant. This was confirmed by the Court of Appeal in Winter v Traditional & Contemporary Contracts Limited. It was held that it is too late to turn the clock back and allow such compensation to be determined by reference to the "negotiated share approach" using the Stokes principle. Compensation under section 84 is to reflect the impact of the actual development on the objector's property and not the loss of an opportunity to extract a share of the profit to be made from the development. This applied and followed the decisions in re SJC Construction Company Limited's Application and Stockport MBC v Alwiyah Developments . In consequence if apart from the financial benefit there are no practical benefits then there is a serious risk that the restrictive covenants could be discharged or modified in a manner which defeats the overage entitlement and if any provision is made for compensation it will be much less than the anticipated amount of the overage.

(iii) Uncertainty – the section 84 application in this case was issued in July 2015. The parties now face the prospect of further litigation over the remedies to be awarded by the Courts with regard to the consequences of the cynical breach.

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12. Injunction or compensation – Lord Burrows recognised that the Supreme Court decision was not the end of the litigation. There is outstanding a potential claim for an injunction or alternatively compensation which it was indicated to the Court on behalf of the Charity could go "beyond conventional compensatory damages" and could include an account of profits as well as negotiating damages.

The Supreme Court had firmly rebutted reliance in the section 84 application on Lord Sumption's judgment in Lawrence v Fen Tigers Limited. He stated that the "whole jurisprudence in this area will need one day to be reviewed in this court. There is much to be said for the view that damages are ordinarily an adequate remedy for nuisance and that an injunction should not usually be granted in a case where it is likely that conflicting interests are engaged other than the parties' interests. In particular, it may well be that an injunction should as a matter of principle not be granted in a case where a use of land to which objection is taken requires and has received planning permission. However, at this stage, in the absence of argument on these points, I can do no more than identify them as calling for consideration in a case in which they arise."

The question is whether the future review raised by Lord Sumption will be carried out in any subsequent litigation between these parties.